

Message Text

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SUBJ: NEW ECONOMIC POLICY - INDIAN VERSION

1. FOR SEVERAL MONTHS EMBASSY HAS BEEN REPORTING GROWING CRITICISM OF EXISTING GOI ECONOMIC POLICIES BY THE PRESS, ACADEMICS, BUREAUCRATS, AND EVEN THE PRIME MINISTER HERSELF. THIS CACOPHONY REACHED A CRESCENDO IN THE LAST TWO WEEKS WITH REPORTS OF CABINET MEETINGS AND DISCUSSIONS BETWEEN THE PRIME MINISTER AND BUSINESS LEADERS REGARDING CHANGES IN ECONOMIC POLICY. MORE RECENTLY, ATTENTION FOCUSED ON "INFLATION AND INDIA'S ECONOMIC CRISIS", A PUBLIC REPORT BY V.K.R.V. RAO AND FIVE OTHER PROMINENT MODERATE LEFT ECONOMISTS AND REPORTS OF A PARALLEL "PAPER" BY L.K. JHA, P.N. DHAR, AND B.K. NEHRU. RAO REPORT CALLED FOR GREATER USE OF MARKET MECHANISMS IN ALL PHASES OF ECONOMIC POLICY WITH LIBERALIZATION OF CONTROLS ON INDUSTRIAL AND AGRICULTURAL PRODUCTION AND PRICING. JHA PAPER ALLEGEDLY ALSO CALLED FOR LIBERALIZING RESTRICTIONS ON INVESTMENT OF FOREIGN CAPITAL IN INDIA. RESPONSE BY TRADITIONAL LEFT WAS SPEEDY IN FORM OF CRITIQUE BY FIVE LEFT WING ECONOMISTS AND GROUP OF MILITANT RADICAL

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CONGRESS MPS, BUT APPEARED TO FIND LITTLE ECHO EXCEPT IN

COMMUNIST PRESS.

2. RAO REPORT (DETAILS BY AIRGRAM) FOCUSED ON MASSIVE INFLATION AFFECTING INDIA AND CALLS FOR SERIES OF CHANGES IN POLICY. RECOMMENDATIONS MAY SEEM HIGHLY ORTHODOX BY WESTERN STANDARDS, BUT, IF IMPLEMENTED, WOULD BE REVOLUTIONARY HERE. THEY INCLUDE: (A) SHARP REDUCTION IN GOVERNMENT SPENDING WHICH AUTHORS DESCRIBE AS PRIMARY CAUSE OF INFLATIONARY PRESSURE; (B) INCREASES IN PUBLIC BORROWING TO SOAK UP FUNDS AND SELECTIVE INCREASES IN TAXES ON PROPERTY AND DURABLE CONSUMPTION GOODS TO HIT UPPER CLASSES; (C) ELIMINATION OF WIDESPREAD BUT HAPHAZARD AND UNENFORCEABLE PRICE CONTROLS WHICH HAVE LED TO MASSIVE BLACK MARKET AND REDUCED TAX AND INVESTMENT BASE; (D) INCREASE IN AGRICULTURAL PRICES TO FARMERS AND CONSUMERS FOR PURPOSES OF SECURING INCREASED PRODUCTION AND ELIMINATING BLACK MARKET; (E) LIBERALIZATION OF LICENSING RESTRICTIONS ON INDUSTRIAL PRODUCTION BY PRIVATE SECTOR. ALL OF THESE POLICIES ARE JUSTIFIED AS "SHORT TERM STRATEGY" ON WAY TOWARDS "SOCIALIST" ECONOMY WHICH REMAINS OVERRIDING GOAL.

3. JHA "PAPER" REPORTEDLY MAKES PARALLEL RECOMMENDATIONS FOR LIBERALIZATION OF DOMESTIC ECONOMY BUT GOES ON TO COMMIT ULTIMATE HERESY OF CALLING FOR "BIG INFLOW OF PRIVATE FOREIGN CAPITAL, PARTICULARLY FROM MULTINATIONAL GIANTS". COMING FROM SUCH PROMINENT INDIVIDUALS AS DHAR (PRIME MINISTER'S PRIVATE SECRETARY), NEHRU (HIGH COMMISSIONER IN UK) AND JHA (GOVERNOR OF JAMMU AND KASHMIR) NEWSPAPER STORIES QUICKLY DREW OFFICIAL GOVERNMENT DENIAL THAT SUCH RECOMMENDATIONS HAD BEEN CONSIDERED BY CABINET. WHILE RUMORS AS TO NATURE OF REPORT RECOMMENDATIONS CONTINUE TO ABOUND, EMBASSY CONTACTS STATE THAT NO SUCH PAPER EXISTS. MOST LIKELY PAPER DOES NOT EXIST BUT SUBJECT HAS BEEN DISCUSSED AT CABINET LEVEL.

4. EVEN PLANNING MINISTER D.P. DHAR, SUFFERING AT LEAST A TEMPORARY POLITICAL ECLIPSE, FELT CONSTRAINED ON THE EVE OF RELEASING 5TH FIVE YEAR PLAN TO JOIN CALL FOR INCREASED PRODUCTION AND REDUCED GOVERNMENT SPENDING. HE CALLED FOR MEASURES TO "INDUCE AND EVEN TO COERCE PRIVATE INVESTMENT", BUT INDICATED THAT THE PLAN WILL ONLY BE SLIGHTLY REDUCED LIMITED OFFICIAL USE

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FROM LEVELS ENVISAGED IN THE APPROACH DOCUMENT EARLIER THIS YEAR.

5. IN MEETING WITH AMBASSADOR, G.D. BIRLA CONFIRMED MEETING WITH PRIME MINISTER AND HER REQUEST FOR RECOMMENDATIONS FOR NEW POLICIES TO STIMULATE ECONOMY. BIRLA RESPONSE WAS LESS THAN CLEAR, BUT HE NOTED THAT HIS AND OTHER INTERESTS HAD RECEIVED MAJOR INCREASES IN INVESTMENT LICENSES. WHETHER

THESE WILL BE UTILIZED DEPENDS LESS ON CAPITAL AVAILABILITY (THOUGH PRIME INTEREST RATE HAS SOARED TO CLOSE TO 12 PERCENT DUE TO HIGH RESERVE RATIOS) THAN ON PROBLEMATIC WILLINGNESS OF PRIVATE SECTOR TO ACCEPT GOI FINANCIAL ASSISTANCE IN VIEW OF LINGERING FEAR OF GOI INTERFERENCE IN MANAGEMENT AND, ULTIMATELY, THREAT OF SOME DEGREE OF GOI EQUITY INVOLVEMENT.

6. COMMENT: PUBLIC DEBATE WILL NO DOUBT CONTINUE FOR SOME TIME EVEN AFTER RELEASE OF 5TH FYP. WHILE VIRTUALLY ALL GOI LEADERS HAVE CLIMBED ON BANDWAGON OF CRITICISM OF PAST POLICIES AND NEED TO COUNTER INFLATION, LIKELY OUTCOME IN INDIAN CONTEXT IS LITTLE NOTICEABLE CHANGE IN FORMAL POLICY. MOST THAT CAN BE EXPECTED IS SOME LIGHT TRIMMING IN FYP, CONTINUED BUDGETARY CUTS (BOTH PROBABLY IN WRONG AREAS), AND A REDUCED EMPHASIS ON NET ZERO FOREIGN AID.

7. IN THE REAL WORLD INFORMATION IS FRAGMENTARY, BUT THERE APPEARS TO HAVE BEEN SOME LIBERALIZATION OF DOMESTIC INVESTMENT LICENSING, SIGNIFICANT IMPROVEMENT IN PRICING POLICIES, BUT NO FUNDAMENTAL CHANGE IN ATTITUDE TOWARDS FOREIGN INVESTMENT. FOREIGN INVESTMENT POLICY IS LIKELY TO CONTINUE TO BE AMBIVALENT WITH SOME JOINT VENTURES ENCOURAGED TO INCREASE PRODUCTION AT THE SAME TIME THAT OTHERS FACE PRESSURE TO DILUTE EQUITY OWNERSHIP AND RESTRICT PAYMENTS FOR FOREIGN TECHNOLOGY.

8. IN THE AGRICULTURAL SECTOR THE COMBINATION OF EXCELLENT RAINFALL AND HIGH SUPPORT AND PROCUREMENT PRICES SHOULD PRODUCE AND EXCELLENT CROP AND A REDUCTION IN INFLATIONARY PRESSURE. INDUSTRIAL RESPONSE TO GOI OVERTURES REMAINS MUCH MORE UNCERTAIN AND WILL BE INFLUENCED BY THE BIG HOUSES' APPRAISAL OF THE LONG TERM DIRECTION OF GOI POLICY; CHANGE IN FORMAL GOVERNMENT POLICY, IF ANY, WILL ONLY FOLLOW AFTER PROLONGED AND CAREFUL PREPARATION OF POLITICAL CLIMATE AND IS LIKELY TO BE LIMITED OFFICIAL USE

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